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Attorney Work Product

Draft: March 22, 2001

ACTION MEMORANDUM

March 22, 2001

TO: The Commission

FROM: Division of Enforcement

SUBJECT: In the Matter of Trading in the Securities of Bankers  
Trust Corp., File No. HO-3580

RECOMMENDATION: That the Commission:

- (1) authorize the staff to file a civil action against:  
Deutsche Bank, AG, and Rolf-E Breuer, seeking  
injunctive relief and a civil penalty pursuant to  
Section 21(d) of the Securities Exchange Act of  
1934 ("Exchange Act") for violations of Section  
10(b) of the Exchange Act, and Rule 10b-5  
promulgated thereunder; and
- (2) authorize the staff to enter into settlement  
negotiations with the proposed defendants.

ACTION REQUESTED BY: Regular Calendar

PRIOR COMMISSION  
ACTION: On August 29, 1999, the Commission issued a Formal  
Order of Private Investigation.

SOURCE OF CASE: Referral from the New York Stock Exchange.

SMALL ENTITY STATUS: Not applicable

TENTATIVE SUNSHINE  
ACT STATUS: Closed pursuant to 17 C.F.R. 200.402(a)(5),(7) and (10)

OTHER DIVISIONS AND  
OFFICES CONSULTED:

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Office of Economic Analysis  
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## **I. SUMMARY**

This recommendation involves a material misstatement made by Dr. Rolf Breuer, ("Breuer"), Spokesman of the Group Board (equivalent to the CEO) of Deutsche Bank A.G. ("Deutsche Bank"), to a German news magazine in which he falsely denied the existence of takeover talks between Deutsche Bank and Bankers Trust Co. ("Bankers Trust"). At the time of the denial, talks between the two companies were in fact, ongoing. During the few days prior to Breuer's denial of talks, the stock price of Bankers Trust had risen sharply as a result of a financial press report that Deutsche Bank and Bankers Trust were having preliminary takeover talks. Faced with the rising price of his acquisition target, Breuer then publicly denied the existence of takeover talks between the two companies. As a result of that denial, the stock price of Bankers Trust dropped back down. Four weeks after Breuer's denial, the two companies announced that Deutsche Bank would acquire Bankers Trust.

During the summer of 1998, Deutsche Bank reviewed its strategic alternatives and determined that an acquisition of an American financial institution was necessary to meet its strategic goals. At that time, Deutsche Bank publicly expressed its plans to make a U.S. acquisition, but the bank did not specify a target. Deutsche Bank next analyzed five American financial institutions as potential acquisition targets, including Bankers Trust. In July 1998, high-ranking executives from Deutsche Bank met first with the CEO of Bankers Trust and then with Bankers Trust's head of Investment Banking, and discussed a possible combination of the two companies. Both times, Bankers Trust declined to enter into further talks stating that it intended to pursue a stand-alone strategy. This was consistent with publicly disclosed statements made by Bankers Trust in December 1997 that it intended to remain independent. Despite its stated decision to stand alone, however, Bankers Trust was internally analyzing other strategic alternatives. One of these alternatives was a merger with one of various financial institutions, including Deutsche Bank, among others.

In late August and September 1998, a default in the Russian bond market triggered a worldwide financial crisis. Bankers Trust, like many large financial institutions, incurred substantial losses as a result of the ensuing market turmoil. The price of its stock fell from over \$110 per share to prices in the range of \$50-60 per share. Its losses from the market turmoil exceeded \$400 million. By October 1998, Bankers Trust's fortunes were significantly reduced from earlier in the year.

In mid-September of 1998, Deutsche Bank hired Goldman Sachs & Co. ("Goldman"), to advise it on strategic matters and also retained Cleary, Gottlieb, Steen and Hamilton ("Cleary, Gottlieb") to act as legal adviser in a possible business combination. On September 24, 1998, Deutsche Bank decided on Bankers Trust as its primary acquisition target. Breuer then arranged to meet with Frank Newman, President, CEO and Chairman of Bankers Trust. On October 5, 1998, Breuer and Newman met in Washington, DC, and discussed a possible combination of their two companies. At the meeting, Breuer asked Newman if he would meet again to talk further about a possible combination. Newman said he would discuss the proposal with his board. The Bankers

Trust board agreed with Newman that he should pursue talks with Deutsche Bank, and on October 12, 1998, Newman accepted Breuer's invitation to further discuss a combination. Accordingly, in mid-October, 1998, a meeting was scheduled for October 25, 1998 in Frankfurt, Germany.

Between the two meetings on October 5<sup>th</sup> and 25<sup>th</sup>, Deutsche Bank and Goldman worked toward a potential acquisition of Bankers Trust, including the development of proposals to finance the transaction. During this period, Ken Wilson, Deutsche Bank's lead adviser at Goldman, communicated and met with Frank Newman and others at Bankers Trust to help prepare Breuer for the October 25<sup>th</sup> meeting with Newman. Bankers Trust, during this time, also began to focus on a combination with Deutsche Bank and sometime in early to mid-October 1998, hired Morgan Stanley Dean Witter & Co., ("Morgan Stanley") to advise it on strategic matters. In mid-October, Bankers Trust retained Wachtell, Lipton, Rosen & Katz ("Wachtell, Lipton"), to act as legal adviser in a possible business combination. By mid-October, it became clear to Bankers Trust that a merger with Deutsche Bank was a very attractive and concrete strategic alternative. At a board meeting on October 20<sup>th</sup>, the Bankers Trust board decided that it would be prudent for Newman to pursue further talks about a combination with Deutsche Bank. As further evidence of its growing interest in a combination with Deutsche Bank, on October 23<sup>rd</sup>, Bankers Trust shared with Goldman data about its capital and risk-weighted assets, including some of its non-public financial information.

On October 20, 1998, a few days before the October 25<sup>th</sup> meeting between Breuer and Newman, the *Financial Times* published an article stating that Deutsche Bank and Bankers Trust were having preliminary takeover talks. On the day the article was published, Bankers Trust's stock price rose over \$4 or 7%, and continued to rise over the next few days. Both Deutsche Bank and Bankers Trust declined to comment on the article.

On Thursday, October 22, 1998, the German news magazine *Der Spiegel* interviewed Breuer for an article that it published on Monday, October 26<sup>th</sup>. When asked by *Der Spiegel* whether Deutsche Bank was having discussions with Bankers Trust, Breuer responded, "In this industry everybody speaks with everybody. But there were no takeover talks." On October 26<sup>th</sup>, the financial press widely reported on the *Der Spiegel* article and interpreted Breuer's statements as a denial of the existence of takeover talks between Deutsche Bank and Bankers Trust. As a result, the price of Bankers Trust's stock dropped \$4 or 6% for the day.

Breuer's statement was materially false and misleading. By October 22, 1998, Deutsche Bank had targeted Bankers Trust for acquisition and had initiated a CEO to CEO dialogue toward a takeover. Bankers Trust, weakened by the financial crises of August and September 1998, had authorized its CEO to pursue the possibility of a combination with Deutsche Bank. Both banks had retained investment bankers and legal advisers. Deutsche Bank was not seeking to acquire any other U.S. bank and Bankers Trust was not seeking to contact any other potential merger partner.

Since both banks were now focusing on each other as potential merger partners, and both had taken significant, affirmative steps toward a combination, the existence of their dialogue would have “assumed actual significance in the deliberations of a reasonable shareholder.” Basic, Inc. v. Levinson, 485 U.S. 224, 231-32 (1988). Indeed, the rise in the price of Bankers Trust’s stock after the *Financial Times* reported the existence of preliminary takeover talks evidences the materiality of this information to investors. Further, the drop in the price of Bankers Trust’s stock after the denial of takeover talks in *Der Spiegel* evidences the materiality of the denial.

On Sunday October 25, 1998, three days after *Der Spiegel* interviewed Breuer, and the day before the interview was published, Breuer and Newman met again in Frankfurt, Germany at Breuer’s home. The two discussed in more depth a possible combination of their two companies and Breuer made clear to Newman that Deutsche Bank was interested in either a merger with, or acquisition of, all of Bankers Trust. Breuer asked Newman if he would sign a confidentiality agreement so that the two companies could share non-public financial information. Three days after the meeting, on October 28<sup>th</sup>, Newman informed Breuer that Bankers Trust was willing to share non-public information with Deutsche Bank. Accordingly, Newman and Breuer met again in New York on November 2<sup>nd</sup> and a confidentiality agreement was signed on November 6<sup>th</sup>. Due diligence was conducted and on November 23<sup>rd</sup>, less than one month after Breuer’s denial to *Der Spiegel*, Deutsche Bank and Bankers Trust announced that, pending approval of their boards, they had reached an agreement whereby Deutsche Bank would acquire all of Bankers Trust’s stock for \$93 per share in cash.

The staff recommends that the Commission authorize and institute a civil action against Deutsche Bank and Rolf Breuer for violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and seek injunctive relief and a civil penalty. The staff also recommends that the Commission authorize it to enter into settlement negotiations with the proposed defendants.

## **II. ISSUE PRESENTED**

**Issue:** Was Breuer’s statement denying takeover talks between Deutsche Bank and Bankers Trust a knowing material misstatement?

**Answer:** Yes. Beginning in early October 1998, Deutsche Bank and Bankers Trust were engaged in CEO to CEO talks about combining their companies. Both had retained investment bankers and legal advisers, and both were focusing on a combination with each other, and not with other merger partners. On October 22, 1998, when Breuer made the statement, he knew he was scheduled to meet again with Newman on October 25, 1998, at which time he would aggressively continue his pursuit of Bankers Trust. On October 20<sup>th</sup> the *Financial Times* published an article reporting that Deutsche Bank and Bankers Trust were having preliminary takeover talks. This article caused the price of Bankers Trust’s stock to rise over \$4 or 7% on the day of publication and it continued to rise in the following days. In an apparent attempt to contain the rise in the stock price of his target, Breuer denied the existence of takeover talks between Deutsche Bank and

Bankers Trust in an interview with *Der Spiegel* magazine, conducted on October 22<sup>nd</sup> and published on October 26<sup>th</sup>. Breuer's denial caused the price of Bankers Trust's stock to drop back down \$4 or 6% on the day of publication. The evidence makes clear that Breuer's denial of takeover talks was false and material and that Breuer possessed the intent and motive to mislead the public.

### **III. PROPOSED DEFENDANTS**

A. **Deutsche Bank, A.G.**, a banking company with limited liability organized under the laws of the Federal Republic of Germany, is Germany's largest bank and is headquartered in Frankfurt, Germany. The common stock of Deutsche Bank is listed on the Frankfurt Stock Exchange. Deutsche Bank is the parent company of a conglomerate consisting of banks, capital markets companies, funds management companies, mortgage banks and a property finance company, installment financing and leasing companies, insurance companies, research and consultancy companies and other domestic and foreign companies.

B. **Rolf-E. Breuer**, age 63, a resident of Germany, is the Spokesman of the Group Board of Deutsche Bank, AG (the equivalent of an American CEO). Breuer has a law degree and an advanced law degree.

### **IV. RELATED PARTIES**

A. **Bankers Trust Corp.**, during the relevant time period, was a bank holding company organized under the laws of the state of New York with headquarters in New York, NY. Bankers Trust had common stock registered with the Commission pursuant to Section 12(b) of the Exchange Act and was listed on the New York Stock Exchange. Bankers Trust was also a bank holding company registered with the Federal Reserve Board.

B. **Frank N. Newman**, age 58, a resident of New York, New York, during the relevant time period was the President, Chief Executive Officer and Chairman of the Board of Bankers Trust Corp.

### **V. FACTS**

#### **A. Deutsche Bank's Early Interest in Bankers Trust**

During the spring and summer of 1998, Deutsche Bank reviewed its position in the banking sector both in Europe and internationally and determined that it had to strengthen its position in the United States. Deutsche Bank evaluated numerous U.S. companies as possible combination partners and in July 1998, narrowed its list of candidates to five, including Bankers Trust, to which it assigned the code name, "Liberty". Particularly impressed with the strategic fit of Bankers Trust, executives from Deutsche Bank contacted and met with executives from Bankers Trust twice in July 1998 to discuss a possible combination of the two companies. On July 16, 1998, Ronaldo

Schmitz, head of the North America region of Deutsche Bank's Global Corporates & Institutions, met with Frank Newman.<sup>1</sup> On July 23, 1998, the head of Global Markets at Deutsche Bank met with the head of the Investment Banking Division at Bankers Trust. On both occasions, Bankers Trust declined Deutsche Bank's invitation to talk further about a combination.

During the spring and summer of 1998, Bankers Trust also evaluated its business strategy and considered as one possibility, some form of combination with another bank, including Deutsche Bank. In June 1998 however, with its stock trading near its year high, Bankers Trust decided to pursue a stand-alone strategy.<sup>2</sup> Despite this decision, Bankers Trust continued to analyze other strategic alternatives including a merger with Deutsche Bank.<sup>3</sup>

Although the banks had some interest in each other, in the summer of 1998, neither Deutsche Bank nor Bankers Trust was particularly focused on a combination with the other. In early September 1998, Breuer publicly expressed Deutsche Bank's plans to expand in the United States by acquiring a U.S. bank, but he did not specify any particular bank.<sup>4</sup> Likewise, Bankers Trust, as mentioned above, expressed in public its intent to stand-alone. In December 1997, Frank Newman publicly stated, "Bankers Trust is not for sale",<sup>5</sup> and Bankers Trust made no public statements to the contrary throughout the summer of 1998.

#### **B. Deutsche Bank Decides to Act to Acquire Bankers Trust**

In early September of 1998, after conducting further analyses, Deutsche Bank concluded that to meet its global aspirations in wholesale banking it had to pursue a

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<sup>1</sup> Deutsche Bank provided Schmitz with various documents to prepare for the meeting including a packet called, "Project Liberty; Short Profile for Discussion" dated July 14, 1998, which discussed the merits of a merger between Deutsche Bank and Bankers Trust. The document noted the potential synergies and strategic fit of the two companies and assessed the transaction mechanics of a merger.

<sup>2</sup> The price/volume trading history of Bankers Trust stock from January 1 through December 31, 1998, is attached as Appendix A. The stock hit its 1998 high of \$136 5/16 on April 22, 1998. In June and July 1998, the stock traded from \$110 to \$122 15/16.

<sup>3</sup> A Bankers Trust document called, "Osprey, Preliminary Analysis" dated July 30, 1998 contained dilution analyses assuming Deutsche Bank acquired Bankers Trust. Additional Bankers Trust documents dated August 7 and August 26, 1998, also analyzed financial considerations and synergies of an acquisition of Bankers Trust by Deutsche Bank. Despite that Bankers Trust said it was reviewing a variety of strategic alternatives regarding Deutsche Bank, it appears that all of the analyses of Deutsche Bank created by Bankers Trust evaluate only a merger or acquisition.

<sup>4</sup> *Deutsche Bank's Breuer Aims to be Able to Move Quickly on U.S. Acquisition*, AFX News, September 8, 1998.

<sup>5</sup> *Flying Frank Puts the Trust Back Into Bankers Trust: Scintillating Deals and a Strong Share Price Have Restored the Bank's Credibility and Transformed the Chairman*, Financial Times (London), December 30, 1997.

“rigorous acquisition process” in the United States. This was necessary in part because of the defection in July 1998 of most of the technology team of Deutsche Bank’s investment banking group, which left the bank particularly weak in the United States. Deutsche Bank also faced possible serious competition in Europe from U.S. investment banks because of the imminent introduction of the Euro. Therefore, to pursue its goal of strengthening its global position and expanding in the United States, on September 12, 1998, Deutsche Bank hired Goldman Sachs & Company to advise it on strategic matters including a possible merger with a U.S. company. On September 18, 1998, Deutsche Bank retained Cleary, Gottlieb to act as legal adviser in a possible merger. Shortly thereafter, on September 24, 1998, the executive management of Deutsche Bank decided on Bankers Trust as its only U.S. target because it provided the best potential strategic fit.

Deutsche Bank also determined that in September 1998 the time had come to acquire Bankers Trust. An acquisition of Bankers Trust was now more affordable because the downturn in the financial markets caused by the Asian and hedge fund crises reduced Bankers Trust’s stock to less than half the price at which it traded in July 1998.<sup>6</sup> Thinking that now, Bankers Trust would be more receptive to the possibility of a business combination than it was in the summer, Rolf Breuer called Frank Newman and arranged to meet with him on October 5, 1998, in Washington, DC, at the annual I.M.F. conference.

### **C. Breuer and Newman Have Their First Meeting**

Breuer and Newman met alone on October 5, 1998, in Washington, DC, for approximately one hour in a hotel room reserved by Deutsche Bank.<sup>7</sup> At the meeting, Breuer proposed to Newman that their two companies combine in some form and tried to establish mutual trust so that Newman would agree to further talks. The possible types of combinations discussed at the meeting were not limited to merger or acquisition. However, by October 2, 1998, Deutsche Bank in fact was focused on acquiring all of Bankers Trust. Deutsche Bank had analyzed the financial considerations of an acquisition of Bankers Trust, had concluded that it would have to pay cash for Bankers Trust’s stock, and had begun to evaluate how to raise the capital to finance an acquisition. To assist in conducting this financial analysis, in late September 1998, Deutsche Bank shared with Goldman some of its non-public financial data. Additionally, on October 2, 1998, Goldman placed Bankers Trust on its firm’s “Grey List”, which signified that Deutsche Bank’s undertakings toward Bankers Trust were market sensitive and warranted the placing of restrictions on Goldman’s trading of the stock.

At the October 5<sup>th</sup> meeting, Breuer provided Newman with two documents. The first one, “Joining Forces on a Global Scale, Strategic Benefits of a Partnership Between

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<sup>6</sup> On July 14, 1998, Bankers Trust stock traded at \$122 5/8. It steadily fell during the summer and early fall and on September 24, 1998, traded at \$64 7/16.

<sup>7</sup> Breuer testified that he did not want made public the fact that he and Newman met because it might cause the marketplace to jump to conclusions resulting in a possible rise in the stock price of both banks.



Circle [Bankers Trust] and Cross [Deutsche Bank]”, noted that a combination of the two companies allowed for “critical mass in key businesses” creating a “top 5 global asset manager” and a “top 5 global custodian”. The second one, “Summary Review of Cross’ Strategy and Competitive Position”, described the businesses of Deutsche Bank and provided the bank’s “financial highlights”.

At the conclusion of the meeting on October 5<sup>th</sup>, Breuer invited Newman to engage in further talks. Newman replied that he would discuss the proposal with members of his board and contact Breuer if he desired to talk further about a combination. Because Bankers Trust faced large third quarter trading and hedge fund losses<sup>8</sup>, and because its stock was trading at its year low, Newman recommended to members of the Bankers Trust board that he meet again with Breuer. The board concurred. On or about October 12, 1998, Newman called Breuer and agreed to meet with him again. A second meeting was scheduled for Sunday, October 25, 1998, at Breuer’s home in Frankfurt, Germany.

#### **D. Deutsche Bank is Anxious to Proceed**

By early October 1998, Breuer was very interested in acquiring Bankers Trust. After the October 5<sup>th</sup> meeting, but prior to hearing back from Newman about scheduling a second meeting, Breuer was anxious to learn what Newman thought about his proposal that their companies combine. To gain insight in this respect, Breuer considered contacting Paul Volcker, a Bankers Trust board member whom he knew personally. However, his adviser Ken Wilson of Goldman Sachs, dissuaded Breuer, saying that doing so would hurt the trust relationship Breuer built with Newman at the first meeting. Also in early October 1998, it was rumored that the Federal Reserve Board approached several U.S. banks about acquiring the weakened Bankers Trust. In response to this, Deutsche Bank considered informing the Fed that it was interested in acquiring Bankers Trust, but decided against doing so.

Between the meetings on October 5<sup>th</sup> and 25<sup>th</sup>, Deutsche Bank continued collaborating with Goldman in analyzing the financing of a potential acquisition of Bankers Trust.<sup>9</sup> One document, “Circle/Cross Financing Considerations” dated October 13, 1998, evaluated the financing requirements, alternatives, and implications of an acquisition of Bankers Trust. Another document, “Financing Considerations Regarding Acquisition of Circle” dated October 23, 1998, calculated the total amount of cash

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<sup>8</sup> On September 1, 1998, Bankers Trust announced \$350 million in trading losses principally in Russian securities and ultimately, incurred a \$488 million loss for the third quarter that was announced on October 22, 1998. Bankers Trust also had over \$500 million invested in hedge funds, including Long Term Capital Management. Additionally, on September 24, 1998, Standard & Poor’s downgraded Bankers Trust stock. Lastly, Bankers Trust stock price hit its 1998 low of 49 3/16 on October 7, 1998.

<sup>9</sup> Deutsche Bank’s phone records show that between October 1<sup>st</sup> and October 25<sup>th</sup>, the Deutsche Bank team that was conducting financial analyses for the deal placed at least 32 phone calls to Goldman. Most of those calls were made to the Goldman team in Germany that was conducting financial analyses. The number of calls placed from Goldman’s team in Germany to Deutsche Bank is unknown because Goldman did not retain those phone records.

needed for an acquisition at various prices per share and premiums. It included a feasibility assessment and a recommendation that Deutsche Bank use a rights offering, possibly combined with a market offering, to raise sufficient capital for the acquisition. A rights offering was in fact later used to finance the acquisition of Bankers Trust.

#### **E. Ken Wilson Acts as a Go-between**

Between the October 5<sup>th</sup> and October 25<sup>th</sup> meetings between Breuer and Newman, Ken Wilson, Deutsche Bank's investment banker, communicated numerous times with Newman and Jeffrey Goldstein, a member of the management committee of Bankers Trust who was acting as strategy adviser to Newman. Wilson was a personal friend of both Newman and Goldstein's and acted as a "go-between" between Deutsche Bank and Bankers Trust.<sup>10</sup>

Shortly after the October 5, 1998 meeting, Wilson called Goldstein to inform him that he was advising Deutsche Bank. Goldstein asked Wilson if Deutsche Bank's interest in combining with Bankers Trust was genuine or if it was a mere "fishing exercise". Wilson assured Goldstein that Deutsche Bank's interest was real. To help Breuer prepare for the October 25<sup>th</sup> meeting with Newman, Wilson met with Newman and Goldstein some time between October 12<sup>th</sup> and 15<sup>th</sup> to learn what their views were of a possible transaction with Deutsche Bank, what issues were important to them, and what questions Newman wanted Breuer to answer at the upcoming meeting on October 25<sup>th</sup>. Among other topics, Newman expressed to Wilson that he wanted more information about Deutsche Bank's capital position because he was concerned about Deutsche Bank's low capital ratio and its ability to afford Bankers Trust. Wilson reported back to Deutsche Bank what he learned from Newman and Goldstein.

#### **F. Bankers Trust's Interest in Combination Grows**

As noted earlier, Bankers Trust was hit hard financially during the third quarter of 1998 and it was becoming increasingly doubtful that Bankers Trust could continue to stand alone. Therefore, in early October 1998, Newman began to more seriously consider combining with another company. Newman informed some members of the board about his October 5, 1998 meeting with Breuer, and these board members agreed that Newman should continue discussions about a combination with Breuer. In early to mid-October 1998, Bankers Trust hired Morgan Stanley as its adviser for strategic matters including a possible merger. Also in mid-October, Bankers Trust hired Wachtell, Lipton to act as legal adviser in a possible merger. Morgan Stanley immediately commenced working on a possible combination between Bankers Trust and Deutsche Bank. Morgan Stanley also worked on other potential alternatives, such as a merger with another firm or measures that would allow Bankers Trust to remain independent. However, these other alternatives proved infeasible. By mid-October 1998, it appeared that a merger with Deutsche Bank was a very attractive and concrete strategic alternative,

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<sup>10</sup> The phone records show that between October 5<sup>th</sup> and 25<sup>th</sup> more than 30 phone calls were made between the phone line of Wilson and the phone lines of Goldstein and Newman.

as there were no other merger candidates interested in combining with Bankers Trust.<sup>11</sup> At a board of directors meeting on October 20, 1998, Newman discussed his upcoming meeting with Breuer and the board agreed with him that it would be prudent to have further talks with Deutsche Bank about a possible combination. The board also formed an Ad Hoc Advisory Group to assist Newman with strategic decisions and implementation.

During mid-October 1998, Bankers Trust more extensively analyzed a potential merger with Deutsche Bank. A document called "Osprey Preliminary Combination Analysis", dated October 23, 1998, illustrated the financial implications of an acquisition of Bankers Trust by Deutsche Bank including various pro forma and dilution analyses using both pooling of interests and purchase accounting. A detailed chart of the synergies of a merger was also included in this analysis. To help prepare Newman for his upcoming meeting with Breuer, Bankers Trust prepared a list of questions and issues concerning Deutsche Bank's various divisions, restructuring efforts, and capital position, to be discussed with Breuer.

#### **G. Bankers Trust Shares Some Non-public Financial Data with Goldman**

Another indication of Bankers Trust's growing interest in combining with Deutsche Bank was that on October 23, 1998, Bankers Trust sent to Goldman financial data related to Bankers Trust's third quarter results as well as details of its capital and risk-weighted assets. This information was used by Deutsche Bank to calculate the amount of capital needed to acquire Bankers Trust. Some of the financial data included in the packet sent to Goldman by Bankers Trust was non-public.<sup>12</sup>

#### **H. October 20, 1998 *Financial Times* Article Leaking Takeover Talks Causes Jump in Price of Bankers Trust Stock<sup>13</sup>**

On Tuesday, October 20, 1998, as Newman and Breuer prepared for their upcoming meeting, the *Financial Times* printed an article stating that Deutsche Bank and Bankers Trust were having "preliminary takeover talks". This caused Bankers Trust's stock price to rise \$4 3/16 or over 7% on the day it was printed.<sup>14</sup> Fueled by this article,

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<sup>11</sup> In fact, Donald Moore, the lead investment banker from Morgan Stanley who advised Bankers Trust, testified that going into the October 25<sup>th</sup> meeting with Deutsche Bank, Bankers Trust had no "back-up plan" or second choice it intended to pursue in the event that merger talks between Breuer and Newman failed to proceed to the next level.

<sup>12</sup> The data sent to Goldman included non-public worksheets that calculated Bankers Trust's risk-weighted assets and tiers 1, 2, and 3 capital (i.e., capital calculations required by bank regulations). Goldstein testified that Wilson asked him for data on Bankers Trust's capital position in order to answer Bankers Trust's questions about Deutsche Bank's capital position.

<sup>13</sup> The October 20, 1998 *Financial Times* article is attached as Appendix B.

<sup>14</sup> See, attached as Appendix C, Memorandum dated July 14, 2000, from William Dale and Anthony Homan, S.E.C. Office of Economic Analysis ("OEA"), which concludes that the rise in the stock price of Bankers Trust following the publication of the October 20<sup>th</sup> *Financial Times* article is consistent with a

the price continued to rise over the next few days and closed on Friday, October 23<sup>rd</sup> up \$12 1/8 or over 22% for the week.<sup>15</sup>

At the time it was published, both Deutsche Bank and Bankers Trust declined to comment on the *Financial Times* article. In testimony, Wilson said that when this article was published, both Deutsche Bank and Bankers Trust were concerned that the other side had "leaked". Newman and Breuer however, both testified that the article was inaccurate and characterized what was transpiring between the two companies as "exploratory talks" about a possible combination, and not as "preliminary takeover talks", as the article reported.<sup>16</sup> Newman testified that at the time this article was published, he did not have a clear understanding of what type of combination Deutsche Bank intended and therefore, he would not describe the talks as "takeover" talks. Breuer testified, contrary to other evidence, that Deutsche Bank had not yet decided that a total acquisition of Bankers Trust was what it wanted so he would not describe the talks as "takeover" talks.

Although Breuer claimed the article was inaccurate, he testified that he was "angry" when he read it because he "thought it was not helpful to pursue our discussions with Bankers Trust in a smooth and trustworthy way." Although he would not describe his October 5<sup>th</sup> meeting with Newman as a "takeover talk", Breuer admitted that he did not want any publicity of the fact that the two of them had met alone, "face-to-face", and the fact that Deutsche Bank "was interested in continuing those talks", leaked to the public, because it might lead the market to draw premature conclusions and inflate Bankers Trust's stock price. In fact, in testimony Breuer acknowledged that the rise in Bankers Trust's stock price that occurred on the day the article was published was "logical" because, he said, the market believed the "rumor" about takeover talks between the two companies was true.

#### **I. Breuer and Newman Meet Again on Sunday, October 25, 1998 in Frankfurt<sup>17</sup>**

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finding that the report of takeover talks between Deutsche Bank and Bankers Trust was considered material information to the marketplace.

<sup>15</sup> The price of Bankers Trust's stock continued to rise in the days after the publication of the *Financial Times* article despite that on October 22, 1998, Bankers Trust announced third quarter losses totaling \$488 million and announced that it held investments of \$300 million in Long Term Capital Management and \$225 million in other hedge funds.

<sup>16</sup> Newman discussed the *Financial Times* article at the Bankers Trust board of directors meeting on October 20, 1998 and a copy of the article was provided to each director.

<sup>17</sup> Donald Moore, the lead investment banker at Morgan Stanley advising Newman, traveled from London to Frankfurt and met with Newman for over six hours on October 24<sup>th</sup> to help prepare Newman for the meeting with Breuer. Moore reviewed with Newman a document created by Morgan Stanley called "Project Eagle (Bankers Trust) Briefing Materials" dated October 24, 1998, which discussed Deutsche Bank's businesses and evaluated a possible merger of the two banks. Also, Goldman and Deutsche Bank, in preparation for the October 25<sup>th</sup> meeting, collaborated on an outline of a potential script for Breuer dated October 23, 1998, which included the statement that Deutsche Bank had thought a lot about how it would finance an acquisition of Bankers Trust and decided that it would raise most of the capital for the acquisition through a rights offering. This was in fact the means that Deutsche Bank ultimately used to

On Sunday, October 25, 1998, Breuer and Newman met again alone at Breuer's home in Frankfurt, Germany for about three hours.<sup>18</sup> At the meeting the two discussed the strengths and weaknesses of their companies and spoke more extensively about combining their businesses. Newman testified that at the meeting he learned from Breuer that Deutsche Bank was interested in either a merger with, or acquisition of, the whole of Bankers Trust and Breuer described to him how Deutsche Bank envisioned running the combined businesses. Although a specific role for Newman was not discussed, Breuer indicated to Newman that he intended for Newman to play an important role in the combined company.

At the end of the meeting, Breuer asked if Newman would meet with him again to sign a confidentiality agreement so that the companies could exchange non-public information. Breuer suggested that they meet again on November 2, 1998 in New York, because Breuer would already be in New York on other business. Newman said he would discuss the proposal with his board. On October 28<sup>th</sup>, Newman informed Breuer that Bankers Trust was willing to exchange confidential information and a third meeting between Newman and Breuer was scheduled for Monday, November 2<sup>nd</sup> in New York.

**J. Breuer Denies Takeover Talks Causing a Drop in Price of Bankers Trust's Stock**

On October 22, 1998, three days before the second meeting between Breuer and Newman, the German news magazine *Der Spiegel* interviewed Breuer for an article it published on Monday, October 26, 1998.<sup>19</sup> During the interview, *Der Spiegel* asked Breuer about Deutsche Bank's interest in expanding in the United States and specifically, about its interest in Bankers Trust. The following is an excerpt from the article translated from German:<sup>20</sup>

**Der Spiegel:** Are you interested in the American investment bank, Bankers Trust, as was written this week?

**Rolf Breuer:** There isn't anything that I can relate to the shareholders.

**Der Spiegel:** But you have had discussions with the Americans?

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finance the acquisition of Bankers Trust. Also contained in the potential script was a preliminary rough offer price of \$75 per share or a premium of 50% for all of Bankers Trust's stock.

<sup>18</sup> Breuer testified that he scheduled the meeting to occur at his home so that he and Newman would not be seen together and to preserve confidentiality. Presumably, also to preserve confidentiality, Newman and Jeffrey Goldstein, who went with Newman to Germany, traveled to Frankfurt by private plane and left from Teterboro airport instead of Kennedy International. In addition, apparently to avoid the risk of being seen leaving together from the Bankers Trust offices, Newman and Goldstein were each picked up from their respective homes in New York City on Friday evening, October 23, 1998, and transported to the airport.

<sup>19</sup> The *Der Spiegel* article and various financial press reports about the article are attached as Appendix D.

<sup>20</sup> In this Memorandum, the English translation of the excerpt that Breuer provided in testimony is used.

**Rolf Breuer:** In this industry everybody speaks with everybody. But there were no takeover talks.

**Der Spiegel:** But Bankers Trust lets you take a peek in their books?

**Rolf Breuer:** No. That would already be pillow talk.

The day after the interview, on October 23<sup>rd</sup>, *Der Spiegel* provided to Breuer a draft of the interview for him to review and edit. Breuer testified that he did make some corrections to the draft, but that the above-excerpted section required no editing as it was complete and accurate<sup>21</sup>.

On October 26<sup>th</sup>, various English-language business publications reported on the *Der Spiegel* article and interpreted Breuer's statements as a denial of the existence of takeover talks between Deutsche Bank and Bankers Trust. As a result of the denial, the price of Bankers Trust's stock fell \$4 on October 26<sup>th</sup>, from \$66 7/8 to \$62 7/8, or down 6% for the day.<sup>22</sup>

Breuer testified that in the above-excerpted section of the interview, he understood *Der Spiegel* to be persistently inquiring in three separate ways about the takeover talks reported in the recent *Financial Times* article. Despite his actual choice of words, Breuer said that he intended each response to *Der Spiegel*'s questions to mean "no comment". He explained that he did not use the actual words "no comment" because he said doing so is considered "blunt", "impolite", or "arrogant". He added that repeating "no comment" to each of the *Der Spiegel* questions might have made the public suspicious that he had something to hide.

Breuer's contention that saying the actual words "no comment" is considered "blunt", "impolite" or "arrogant", is contradicted however, by his earlier testimony. When Breuer testified about the communication policy at Deutsche Bank, of which he is in charge, he said that responding "no comment" to the press regarding inquiries about merger talks was not considered rude in Germany both in 1998 and today. In fact, Breuer said that answering "no comment" when asked about merger rumors is Deutsche Bank's current policy and was its policy in 1998.<sup>23</sup>

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<sup>21</sup> Although Breuer testified that he reviewed and edited only one draft of the *Der Spiegel* article, the bank was given a second opportunity to review a draft of the article after *Der Spiegel* incorporated Breuer and the bank's first set of revisions. Dierk Hartwig, Deutsche Bank's Chief Press Officer, reviewed and edited both drafts of the article and in a cover letter to *Der Spiegel* stated that once the bank's revisions were made, *Der Spiegel* had Deutsche Bank's permission to print the article. Breuer testified that Deutsche Bank and *Der Spiegel* had an unwritten agreement that *Der Spiegel* would not print the article without Deutsche Bank's permission.

<sup>22</sup> See OEA Memorandum attached as Appendix C, which concludes that the drop in price of Bankers Trust stock following the publication of Breuer's denial in *Der Spiegel* is consistent with a finding that Breuer's denial of takeover talks between Deutsche Bank and Bankers Trust was considered material information to the marketplace.

<sup>23</sup> Citing bank policy, Deutsche Bank officially declined to comment about merger rumors on many occasions including the following: in November 1998, after a barrage of merger rumors surfaced just prior to its announcement to acquire Bankers Trust; in October 1998, after the *Financial Times* article reported

Breuer testified that at the time of the *Der Spiegel* interview, he did not consider the talks he was having with Bankers Trust to be "takeover talks", but instead, "exploratory talks" about a possible combination.<sup>24</sup> Even so, he said that he did not intend his answers to be an acknowledgement that Deutsche Bank and Bankers Trust were in fact talking, but were not yet having "takeover talks". Nor did he intend his answers to be a denial that there had been any talks between the two companies. Instead, Breuer said he intended each of his above-excerpted answers as merely a "more polite form of saying 'no comment'".

Despite what Breuer said he intended his answers to mean, the financial press reporting on the *Der Spiegel* article all interpreted Breuer's statements as a denial of takeover talks between Deutsche Bank and Bankers Trust, and not as a 'no comment'. In fact, in testimony, Tillmann Lauk and Axel Wieandt, Deutsche Bank's head and deputy head of Global Corporate Strategy and advisers to Breuer, both interpreted Breuer's answers to *Der Spiegel* as a denial of takeover talks between Deutsche Bank and Bankers Trust and not as a "no comment". In addition, Wilson, Deutsche Bank's investment banker at Goldman, interpreted Breuer's statements as a denial of takeover talks and testified that he was concerned Deutsche Bank might be "pulling the plug on this deal".

Nevertheless, Breuer testified that he believed his answers were clear and complete and he never considered making a clarifying statement after the interview was published. Breuer did acknowledge in testimony however, the possibility that a reasonable investor might interpret his answers to *Der Spiegel* as a denial of the report of takeover talks that appeared in the October 20<sup>th</sup> Financial Times article. That possibility proved a reality when the price of Bankers Trust's stock dropped \$4 or 6% on the day the *Der Spiegel* interview was published.<sup>25</sup>

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takeover talks between Deutsche Bank and Bankers Trust; in May 1998, after published speculation that Deutsche Bank planned to merge with Chase Manhattan Corp.; in February 1998, after reports that it intended to merge with Credit Suisse; in December 1997, after rumors it might bid for Commerzbank; and in November 1997, after reported rumors it might bid for Banque Nationale de Paris.

<sup>24</sup> Interestingly, Wilson, Breuer's lead adviser, described the talks at this point as "in advanced stages". Wilson said that he was "blindsided" by Breuer's statements in *Der Spiegel* and was very concerned about them. When asked if he thought Breuer's statements were misleading, Wilson testified, "I would categorize (them) as inconsistent with what was actually going on. I think the record shows that the transaction was proceeding and - I am, to this day, at a loss (sic) for what was actually said and why". Wilson expressed his concern about Breuer's statements to Cleary Gottlieb, Deutsche Bank's attorneys, and to Tillmann Lauk, Deutsche Bank's Global Head of Corporate Strategy and Breuer's adviser. Lauk testified that it is possible that he had a discussion with Ken Wilson about the *Der Spiegel* article but that he does not recall it.

<sup>25</sup> The price of Bankers Trust stock dropped another \$2 ¼ the next day, October 27, 1998, after *USA Today* erroneously reported that at the October 20, 1998 Bankers Trust board of directors meeting, Newman told the board that he declined to open merger discussions with Deutsche Bank because Bankers Trust was in a weak negotiating position due to its large third quarter losses. The article said that the board agreed with Newman and unanimously decided that the Bankers Trust was not for sale. Newman testified that the article was inaccurate and that he did not know who the source of the article was.

K. Work Continues and Merger Agreement is Announced on November 23, 1998

Notwithstanding Breuer's statements to *Der Spiegel*, both Deutsche Bank and Bankers Trust continued to analyze a possible merger of their companies and Newman and Breuer met again on Monday, November 2<sup>nd</sup> in New York. At the meeting, Breuer discussed with Newman a preliminary offer price for all of the stock of Bankers Trust. The two agreed to share non-public information and a confidentiality agreement was signed on November 6<sup>th</sup>. On November 23<sup>rd</sup>, Deutsche Bank and Bankers Trust announced that they were in advanced stages of negotiations concerning a cash merger at a proposed price of \$93 per Bankers Trust share. On November 30<sup>th</sup>, after each board approved the agreement, the companies announced that Deutsche Bank was acquiring Bankers Trust for \$93 a share.

VI. LEGAL ANALYSIS

Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit the making of public statements that are materially false or that fail to include facts necessary in order to make the statement made, in the light of the circumstances under which they were made, not materially misleading. E.g., SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 860-2 (2<sup>nd</sup> Cir. 1968) (en banc) cert.denied, 394 U.S. 976 (1969); In the Matter of Carnation Company, Rel. No. 22214 (July 8, 1985). To establish a violation of Exchange Act Section 10(b) and Rule 10b-5, the Commission must prove that the misrepresentations or omissions were material. Texas Gulf Sulphur, 401 F.2d at 848-49. The Commission must also prove that the defendant acted with scienter. Aaron v. SEC, 446 U.S. 680, 691 (1980); See Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193-4 (1976).

A. False or Misleading Statement

Breuer's statement to *Der Spiegel* that "[i]n this industry, everybody speaks with everybody. But there were no takeover talks", was false and misleading.<sup>26</sup> Breuer and

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<sup>26</sup> In this case, Breuer is alleged to have made a material false statement on one occasion. For other cases involving liability for a single false statement, See In the Matter of Bruno, Release No. 40769 (December 10, 1998) (defendant, whose company received and rejected acquisition offer but continued to engage in takeover talks, made false statement to the press that no competitors had made an offer); S.E.C. v. Borman, Lit. Release No.12811 (March 18, 1991) (after the price of his company's stock rose on exceptionally heavy trading, defendant, who was engaged in takeover talks to sell his company, issued press release which falsely stated that he is "aware of the recent activity in the company's stock and knows of no reason for such activity"); S.E.C. v. Trans Global Holding, Inc., Lit. Release No.12775 (February 7, 1991) (involving single press release which falsely stated that defendant was in final stages of obtaining financial backing to make cash acquisition of another company); S.E.C. v. Ball, Lit. Release No. 12242 (September 7, 1989) (defendant issued press release regarding his acquisition offer that contained materially false and misleading statements about his experience as an investor, his prior employment, the existence of merger talks with the target, and the existence of financial backing for the acquisition); S.E.C. v. Muller, Lit. Release No. 11442 (May 28, 1987) (wherein defendant issued acquisition offer containing false statements concerning financial ability to make acquisition and also provided copy of false offer to the press causing rise in stock price of target).



Newman already had met and discussed a possible combination of their businesses; a second meeting between the two was scheduled to occur in three days and efforts had been made to secure the secrecy of both meetings. On numerous occasions, advisers to Deutsche Bank had met and communicated with Newman and other officials at Bankers Trust about a possible combination; each company had hired an investment banking firm and legal advisers to assist it in strategic matters including a possible merger; and each company had completed extensive analyses evaluating a merger between them. Furthermore, Deutsche Bank had targeted Bankers Trust for takeover, and the Bankers Trust board of directors had authorized Newman to pursue talks with Deutsche Bank about a combination.

Breuer could have chosen to answer *Der Spiegel's* questions about Deutsche Bank's interest in Bankers Trust with the actual words "no comment", as was Deutsche Bank's policy and as it had done in the past regarding merger rumors. Instead, Breuer elected to speak and chose words that were understandably interpreted by the financial press, the marketplace and even his own employees and his investment banker, as a denial of the existence of takeover talks between the two companies. Indeed, in a private class action litigation over the facts of this case, the United States District Court for the Southern District of New York held, in denying Deutsche Bank's motion to dismiss, that Breuer's statement to *Der Spiegel* was false and misleading. Buxbaum v. Deutsche Bank, A.G., 2000 U.S. Dist. LEXIS 5838, 98 Civ. 8460 (S.D.N.Y. March 6, 2000)<sup>27</sup> (denying motion to dismiss securities action brought by former shareholders of target company against acquiring company for falsely denying existence of merger negotiations). Accord, In re MCI Worldcom, Inc. Securities Litigation, 93 F.Supp. 2d 276 (E.D.N.Y. 2000); In re Columbia Securities Litigation, 155 F.R.D. 466 (S.D.N.Y. 1994).

## B. Materiality

It is also necessary to demonstrate that Breuer's misstatement was material. A misrepresentation or omission is material if there is a substantial likelihood that under all the circumstances it would have assumed actual significance in the deliberations of a reasonable investor. See Basic, Inc. v. Levinson, 485 U.S. 224, 231-32 (1988); TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976). The materiality of preliminary merger negotiations depends on a balancing of both the probability the merger will occur and the magnitude of its potential impact on a company's fortunes. See Texas Gulf Sulphur, 401 F.2d at 849; Basic, 485 U.S. at 239.

The *probability* that a merger will occur depends on the "indicia of interest in the transaction at the highest corporate levels." Basic, 485 U.S. at 239. As discussed above,

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<sup>27</sup> Buxbaum v. Deutsche Bank is a private class action lawsuit involving the same facts as the instant case brought by former shareholders of Bankers Trust who allege that they sold their stock at an artificially low price after Breuer's false denial of takeover talks to *Der Spiegel* caused a drop in the stock price of Bankers Trust. On March 6, 2000, Judge Koeltl of the United States District Court for the Southern District of New York denied Deutsche Bank's motion to dismiss. The case is pending.

Breuer and Newman, the highest ranking officials at both Deutsche Bank and Bankers Trust, had met and talked about a possible merger; the board of directors of Bankers Trust had encouraged further talks with Deutsche Bank; and the executive management of Deutsche Bank had determined that an acquisition of a U.S. financial institution, specifically Bankers Trust, was strategically necessary. Moreover, Bankers Trust's investment banker acknowledged in testimony that Bankers Trust had no "backup plan" if the Deutsche Bank initiative failed, that there was no other buyer interested in acquiring Bankers Trust, and that no internal strategy was likely to succeed because of its weakened financial state. Thus, the probability of the merger was substantial because of the high level of attention being given to the merger and the absence of any other attractive alternative to the merger.

In addition, and most significantly, by the time Breuer made his statements to *Der Spiegel*, the intentions of the two banks had materially changed from what had been conveyed in the banks' earlier public statements. Deutsche Bank had previously publicly expressed only a general interest in acquiring a U.S. bank without specifying a particular target. But now, Deutsche Bank was exclusively focused on acquiring Bankers Trust. Likewise, Bankers Trust had earlier publicly stated that it was "not for sale", but now, was serious about possibly being acquired by Deutsche Bank. These changes in intentions of the parties, and the concrete steps the two banks had taken in pursuit of those intentions prior to Breuer's interview with *Der Spiegel*, resulted in a significantly different situation with respect to a potential combination than their prior public statements had depicted. Now, there was a considerably greater probability that a merger would occur.

To assess the *magnitude* of a potential merger, consideration should be given to "such facts as the size of the two corporate entities and of the potential premiums over market value." *Id.* Prior to the merger, Deutsche Bank was Germany's largest bank, with total assets of \$627 billion, and Bankers Trust was the seventh largest bank in the United States, with total assets of \$140 billion. Deutsche Bank ultimately agreed to acquire Bankers Trust for \$93 a share in cash for a total of \$10 billion, or at a premium of about 20%.<sup>28</sup> Since Bankers Trust would be entirely acquired, the magnitude of the transaction to Bankers Trust's shareholders is beyond question.

Furthermore, regarding whether the talks were material, because of the effect of a merger on a corporation, negotiations to that end "can become material at an earlier stage than would be the case as regards lesser transactions...." *S.E.C. v. Geon Ind., Inc.*, 531 F.2d 39, 47 (2d Cir.1976); *See also Holmes v. Bateson*, 583 F.2d 542, 558 (1<sup>st</sup> Cir.1978) (merger negotiations material although parties had not yet discussed precise terms); *S.E.C. v. Shapiro*, 494 F.2d 1301, 1306-7 (2d Cir. 1974) (merger negotiations material although they had not jelled to the point where a merger was probable); *S.E.C. v. Gaspar*,

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<sup>28</sup> The closing price of Bankers Trust stock on Friday, November 20<sup>th</sup>, the last trading day before the merger announcement on November 23<sup>rd</sup>, was \$77 1/4. The \$93 per share offer price is a 20% premium over the closing price on November 20<sup>th</sup>. However, during the week prior to the merger announcement, November 16-20<sup>th</sup>, Bankers Trust stock price rose almost \$12 because of merger rumors.

1985 U.S. Dist. LEXIS 20698 (S.D.N.Y. Apr. 16, 1985) (merger negotiations material although they did not proceed to making of actual tender offer).<sup>29</sup> It should be noted that the court in Buxbaum v. Deutsche Bank, *supra*, held in denying Deutsche Bank's motion to dismiss, that the discussions that had already occurred between Deutsche Bank and Bankers Trust prior to Breuer's denial to *Der Spiegel*, were material.

Lastly, in this case, one need not speculate whether Breuer's denial of takeover talks assumed "actual significance in the deliberations of a reasonable investor". Clearly, it did as evidenced by the \$4 or 6% drop in price of Bankers Trust's stock on the day the denial was published. This is supported by the quantitative analysis conducted by the S.E.C. Office of Economic Analysis, which concluded Breuer's denial of takeover talks was considered material information to the marketplace.<sup>30</sup>

### C. **Scienter**

#### 1. **Breuer intended his statements**

Scienter is a state of mind embracing the intent to deceive, manipulate, or defraud. Aaron, 446 U.S. at 686 n.5; Ernst & Ernst, 425 U.S. at 193-94 n.12. The evidence shows that Breuer intended each statement he made to *Der Spiegel*. The day after the interview, *Der Spiegel* provided to Breuer a draft of the interview for him to review and edit. Breuer testified that he did make some corrections to the draft, but that the above-excerpted section in which he denied the existence of takeover talks required no editing as it was complete, accurate and what he intended to say. Even though Breuer asserted in testimony that his words were only another way of saying "no comment", Breuer was not a novice at dealing with the press, but was an experienced corporate spokesman who was in charge of Deutsche Bank's communication policy. Deutsche Bank had answered "no comment" on numerous past occasions in response to merger rumors. It is clear then that Breuer's statement "[i]n this industry, everybody speaks with everybody. But there were no takeover talks," was not an offhand answer made in circumstances under which he had no opportunity for reflection. Instead, Breuer chose the words he used.<sup>31</sup>

#### 2. **Breuer Had a Motive to Deny the Talks**

The evidence shows that Breuer had a motive to artificially deflate the price of Bankers Trust's stock in order to help keep down the acquisition price of his target. "Whatever the exact basis for calculating the ultimate purchase price, it [is] clearly in a

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<sup>29</sup> Although these decisions pre-date the Supreme Court's ruling in Basic v. Levinson, *supra*, they are cited with approval by the Court in Basic and are consistent with the Basic Court's decision to reject a formulaic test of materiality based on price and structure, in favor of the facts and circumstances test of TSC Industries, Inc. v. Northway, Inc., *supra*. See Basic v. Levinson, *supra* at 231-32.

<sup>30</sup> See Appendix C.

<sup>31</sup> Breuer testified in the investigation in English and without a translator present. By all indications, his command of English was excellent and he should have understood how his statement in *Der Spiegel* would translate into English.

purchaser's interest [for] the quoted public price of the asset to be acquired [to be] as low as possible". MCI Worldcom, 93 F.Supp. 2d at 284, quoting, Buxbaum, 2000 U.S. Dist. LEXIS 5838; See also Columbia, 155 F.R.D. at 479-80. "[B]eing able to acquire a company for a significantly reduced price is a sufficient economic benefit to satisfy the motive requirement for scienter." MCI Worldcom, at 284.

In the days just prior to Breuer's denial, the price of Bankers Trust's stock rose considerably as a result of the *Financial Times* article that reported the two companies were having preliminary takeover talks. Breuer admitted in testimony that he was "angry" about this article and that the rise in Bankers Trust's stock price that followed that article was "logical" because investors believed that the article was true. It follows then, that Breuer would have believed that a public denial of those talks would depress the price of Bankers Trust's stock. Given Breuer's keen interest in acquiring Bankers Trust, it is reasonable to infer that he denied the existence of those talks to *Der Spiegel* in order to deflate the stock price and make the intended acquisition more affordable and at a higher premium than if the stock price continued to rise. Breuer even admitted in testimony that it was possible that a reasonable investor might interpret his statements to *Der Spiegel* as a denial of the *Financial Times*' report about takeover talks. Therefore, the evidence shows that Breuer had the motive to deny the talks and an understanding of the impact a denial would have on the stock price.

## VII. RESPONSE TO WELLS

Counsel for Deutsche Bank and Breuer made a Wells Submission on behalf of the bank and Breuer which is attached as Appendix E. The arguments that counsel raises are not persuasive and at times, are contradictory and inaccurate. The staff's comprehensive response to the Wells Submission is attached as Appendix F. The following is a summary of that response.

### A. Counsel Ignores the Totality of Circumstances Test of *Basic v. Levinson*

Deutsche Bank and Breuer argue that by October 22, 1998, the talks between Deutsche Bank and Bankers Trust were not yet material, repeatedly pointing to the absence of any agreement as to price, structure or other specific terms of a merger by that date. However, Deutsche Bank and Breuer ignore the totality of circumstances test for materiality set forth in *Basic* and instead, attempt to advance formulaic tests, an approach that was rejected by *Basic*. Deutsche Bank and Breuer further attempt to trivialize what transpired between the two banks prior to the *Der Spiegel* interview by disregarding or inaccurately describing important facts. However, the facts gathered in the investigation demonstrate that by October 22, 1998, the most important fact of all--the intentions of the two banks--had materially changed from the picture painted by their earlier public statements. In brief, Deutsche Bank had earlier made public statements disclosing a general interest in acquiring a U.S. bank, but not specifying any particular bank. But by October 22, 1998, it had selected Bankers Trust as its target and had taken significant steps toward acquiring it. Bankers Trust, in turn, had previously disclosed an intention to

maintain its corporate independence. However, in October 1998, it altered its firm preference for independence and began seriously exploring the possibility of being acquired by a specific suitor, Deutsche Bank.

These changes of intention are far more important than the existence or non-existence of an agreement as to price, structure or other specific terms. The evolution of a serious interest in a combination created a significant likelihood that a combination would occur. In such a setting, the nonexistence of an agreement on price or structure as of October 22, 1998, is relatively inconsequential because agreement on these specific terms was likely to follow since the parties had developed a significant interest in a combination. That change of intentions and the concrete steps the two banks had taken in pursuit of those intentions were the material undisclosed facts that rendered Breuer's October 22, 1998 statements materially misleading.

**B. Counsel's Argument Regarding Breuer's Statement to *Der Spiegel* is Contradictory and Inaccurate**

**1. Deutsche Bank and Breuer first argue that Breuer meant to disclose that the banks had talked**

Deutsche Bank and Breuer assert that Breuer's statement to *Der Spiegel*, "(i)n this industry everybody speaks with everybody. But there were no takeover talks", was meant by Breuer as a disclosure that Deutsche Bank and Bankers Trust had talked but that the talks were not "takeover talks." For arguments sake, if we assume that Breuer intended his statements as a disclosure of talks, his disclosure was inadequate and materially misleading because it failed to accurately describe what had transpired between the two banks. Breuer's statement implies that a normal degree of communication occurs between companies in the course of their business and that this was the extent of Deutsche Bank's contact with Bankers Trust. As discussed earlier, however, the communications between Deutsche Bank and Bankers Trust at the time Breuer spoke were more than normal business talk.

Moreover, the argument that Breuer intended his statements as a disclosure of talks is unpersuasive and unsupported by the evidence. Breuer's own advisers, Tillmann Lauk and Axel Wieandt in testimony interpreted Breuer's statements as a denial of talks and not as a disclosure of talks. Also, Ken Wilson of Goldman said that when he learned of Breuer's statements, he interpreted them as a denial and thought that Breuer "could have been pulling the plug on this deal." Furthermore, since the publication of Breuer's statements in *Der Spiegel* resulted in a sell off of Bankers Trust's stock with a \$4 drop in price of the stock on the day of publication, it is evident that the marketplace also understood Breuer's words as a denial of takeover talks and not as a disclosure of talks.

Lastly, Breuer himself testified that he did not intend his statement to be an acknowledgement that Deutsche Bank and Bankers Trust were talking to each other. Instead, Breuer testified that he intended his answer to mean "no comment." Thus, their

own client's testimony does not support counsel's argument that Breuer intended his statements as a disclosure of talks.

2. **Counsel's attempt to disprove that Breuer acted with scienter is contradictory**

Deutsche Bank and Breuer attempt to refute that Breuer acted with scienter by arguing that because "*Der Spiegel* did not submit questions to Breuer in advance...there is no reason to believe that Breuer's comments concerning BT were other than spontaneous and off-the-cuff". This argument is disingenuous. First, Breuer testified that he was aware of the October 20, 1998, *Financial Times* article reporting rumors of preliminary takeover talks between Deutsche Bank and Bankers Trust. He should have expected that *Der Spiegel* would follow up on this story by inquiring about discussions with Bankers Trust, and he would have had time to consider how to answer such a question. Moreover, Deutsche Bank and Breuer fail to acknowledge that *Der Spiegel* provided Deutsche Bank with drafts of the interview to edit on two occasions, that Breuer himself did edit some of his statements, and that *Der Spiegel* agreed not to print the interview without Deutsche Bank's approval. Contrary to counsel's assertions, the editing opportunities and the bank's consent to the publication of the interview undermine any claim that Breuer spoke spontaneously, and demonstrates, instead, that Breuer meant what he said.

Deutsche Bank and Breuer further attempt to disprove Breuer's scienter by arguing that he intended his statement to *Der Spiegel*, "(i)n this industry everybody speaks with everybody. But there were no takeover talks", as a "polite no comment." Counsel maintains that "Breuer's intention was to avoid *Der Spiegel's* questions without confirming or denying that any discussions had taken place...." However, this contradicts counsel's earlier assertion that Breuer intended his statements as a disclosure of talks. Either Breuer intended his statements to be a disclosure that talks had occurred between the two banks or he intended his statements to mean "no comment". He cannot have meant both. Counsel here stretches credulity too far.

As noted earlier, Breuer testified that he meant his remark as a way of saying, "no comment." However, he also admitted that a reasonable shareholder could have interpreted his remark as a denial of takeover talks. This admission casts doubt as to whether Breuer's true intention was to say "no comment." Considering that he had and took the opportunity to edit the transcript of the interview before it was published, it is difficult for Breuer to credibly contend that he understood his remarks to mean only "no comment."

C. **Deutsche Bank and Breuer Erroneously Claim that Breuer had no Incentive to Affect Bankers Trust's Stock Price**

Deutsche Bank and Breuer claim that Breuer had no incentive to deflate the price of Bankers Trust's stock when he gave the interview to *Der Spiegel*. However, both the empirical evidence and Breuer's own testimony prove otherwise. Counsel minimizes the

jumps in price of Bankers Trust's stock that occurred on October 20<sup>th</sup> and the days following the *Financial Times* article of October 20<sup>th</sup> that reported the banks were having preliminary takeover talks. On October 20<sup>th</sup>, Bankers Trust's stock closed up over \$4. It continued to rise in the following days and by October 22<sup>nd</sup>, the day of Breuer's interview, it was already up over \$7 for the week. Counsel argues that Breuer had no incentive to deflate Bankers Trust's stock price because he "was not following, and therefore was not aware of, the movement in BT's stock price...." It is incredible that Breuer did not "follow" the price of his potential acquisition, particularly considering Breuer testified that the drop in U.S. bank stock prices after the Russian Federation financial crisis provided "affordability" to any acquisition of a U.S. bank Deutsche Bank made.

When presented in testimony with a trading history of Bankers Trust's stock, Breuer himself acknowledged that the *Financial Times* article caused a run up in the price of Bankers Trust's stock. Of the increase in Bankers Trust's stock price following the article Breuer said that it was "logical" because the market believed the rumor about the existence of takeover talks. It is significant that Breuer acknowledged that the market reacts to merger rumors. It indicates that he should have been aware that the market would react to a denial of rumors. Breuer in fact, admitted as much when he answered that he "cannot exclude" that a reasonable investor could have interpreted his statements, "(i)n this industry everybody speaks with everybody. But there were no takeover talks" to be a denial of the *Financial Times* article.

Counsel emphasizes that Breuer testified he was not sensitive to the fluctuations in the stock price of Bankers Trust because he did not know what the outcome of the talks would be. However, Breuer admitted his sensitivity to the stock price when he testified that if Bankers Trust's stock price continued to run up and it got too expensive, Deutsche Bank would step away from the deal. Breuer denied that the rise in Bankers Trust's stock price after the *Financial Times* article concerned him. However he did acknowledge that if talks developed in the direction of a merger and the rise in price continued, it would affect the final price Deutsche Bank would have to bid for Bankers Trust. The evidence therefore, shows both that the motive existed for Breuer to deflate the price of Bankers Trust's stock, and that Breuer understood the effect a denial of merger rumors would have on the stock price.

#### **D. The Drop in Price of Bankers Trust's Stock on October 26<sup>th</sup> is Statistically Significant and Material**

Lastly, Deutsche Bank and Breuer inaccurately claim that the drop in price of Bankers Trust's stock on October 26<sup>th</sup> was statistically insignificant and immaterial. This claim is rebutted however, by the two quantitative studies conducted by OEA.<sup>32</sup> In its study, Deutsche Bank uses both an inferior model and a less reliable estimation period

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<sup>32</sup> See Appendix C, OEA Memorandum dated July 14, 2000 and See Appendix G, OEA Memorandum dated February 7, 2001.

than OEA uses, which results in less accurate results. These flaws are discussed in the attached OEA analyses.

## **VIII. PROPOSED RELIEF**

### **A. Need for Civil Injunctive Relief and Civil Penalties**

The Commission has the authority to seek and obtain injunctive relief pursuant to Section 21(d)(1) of the Exchange Act upon a showing that (1) violations of the securities laws have occurred, and (2) there is a reasonable likelihood that violations will occur in the future. SEC v. Commonwealth Chemical Securities, Inc., 574 F.2d 90, 99 (2d. Cir. 1978).

In granting or denying injunctive relief, courts have considered the following factors: (1) the egregiousness of the violations; (2) the isolated or repeated nature of the violations; (3) the degree of scienter involved; (4) the sincerity of the defendant's assurances, if any, against future violations; (5) the defendant's recognition of the wrongful nature of his conduct; (6) the likelihood that the defendant's occupation will present opportunities (or lack thereof) for future violations; and (7) the defendant's age and health. See SEC v. Bonastia, 614 F.2d 908, 912 (3d Cir. 1980); SEC v. Commonwealth, 574 F.2d at 100-101.

Rolf Breuer and Deutsche Bank engaged in fraudulent misconduct which justifies the issuance of injunctive relief. As described above, the evidence shows that Breuer acted with scienter when he falsely denied the existence of merger rumors, and that he had the opportunity to edit his statements before they were published. Neither Deutsche Bank nor Breuer has evidenced a recognition that Breuer acted wrongfully, nor have they provided any assurances against future violations. Deutsche Bank has made three major corporate acquisitions in the United States in recent years,<sup>33</sup> and its publicly disclosed corporate strategy is to expand through acquisition. Thus, Breuer and Deutsche Bank may well be in a position to repeat their violations in the future.

Section 21(d)(3) of the Exchange Act authorizes the Commission to seek the imposition of civil penalties when a defendant is found to have violated the Act. The staff recommends that the Commission authorize it to seek civil penalties against Deutsche Bank and Rolf Breuer for the violations discussed above to ensure that they are deterred from future violations and are adequately sanctioned for their violative conduct.

### **B. Disgorgement Should Not be Sought**

The staff recommends that disgorgement not be sought from Deutsche Bank or Breuer. As mentioned earlier, a private class action involving the same facts as the instant case is pending in federal court. The plaintiffs in that case are seeking damages,

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<sup>33</sup> This includes the acquisition of C.J. Lawrence, Inc. in 1989, Bankers Trust Corp. in 1999, and National Discount Brokers Group, Inc. in 2000.



which in this case may reasonably approximate disgorgement, and have made significant progress in that litigation.<sup>34</sup> It is not recommended therefore, that the staff undertake a process that is likely to be duplicative.

#### IV. RECOMMENDATION

Based on the foregoing, the staff recommends that the Commission authorize the above-recommended actions.

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<sup>34</sup> The plaintiffs won on Deutsche Bank's motion for summary judgment of dismissal.